Michigan Economic and Revenue Outlook

FY 2004-05 and FY 2005-06

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EXECUTIVE SUMMARY
January 13, 2005

Revenue Review and Outlook

- FY 2004 GF-GP revenue increased to $8,042.0 million, a 1.0 percent increase over FY 2003. This total is $73.9 million above the December 2004 Consensus estimate. SAF revenue fell 0.9 percent to $10,615.5 million. This total was $63.7 million above the December Consensus estimate. The increase from December was due to accounting adjustments made as part of the FY 2004 book-closing process resulting in higher revenue than was forecast.
- FY 2005 GF-GP revenue is projected to decline 2.1 percent to $7,869.8 million. This total is $31.2 million above the December Consensus estimate. The increase was related to a higher revenue base resulting from the higher than expected FY 2004 revenue totals. SAF revenue is projected to increase 2.5 percent to $10,883.5 million, essentially unchanged from the December Consensus estimate.
- FY 2006 GF-GP revenue is forecast to increase 4.0 percent to $8,181.4 million. This represents a $311.6 million increase over the FY 2005 total. FY 2006 SAF revenue is forecast to grow 4.1 percent to $11,326.5 million. This represents an increase of $443.0 million over the FY 2005 level.

2005 and 2006 U.S. Economic Outlook

- Real Gross Domestic Product growth is forecast to average 3.2 percent in both 2005 and 2006, after increasing by 4.4 percent in 2004.
- After cooling over the summer, national payroll employment strongly increased in October by 312,000 jobs, followed by increases of 137,000 in November and 157,000 in December. Wage and salary employment has grown in each of the past sixteen months, nearly erasing the job losses since the beginning of the last recession. Payroll employment is still about 250,000 below the March 2001 peak. Employment is projected to continue growing over the forecast horizon. The U.S. unemployment rate is forecast to average 5.4 percent in both 2005 and 2006.
- Historically low interest rates have provided consumers with the ability to purchase housing at record levels and refinance existing mortgages. However, with wage and commodity price pressures building, interest rates are projected to increase throughout the forecast period.
- Low capacity utilization rates will constrain investment, but the need to replace increasingly obsolete machinery, tax incentives that allow corporations to repatriate profits from foreign subsidiaries, and higher profits will help spur investment.
- Light vehicle sales are forecast to be 16.7 million units in 2005 and 16.6 million units in 2006, relatively stable from the past two years.
- Consumer price inflation is forecast to be moderate, averaging 2.5 percent in 2005 and 2.4 percent in 2006.

2005 and 2006 Michigan Economic Outlook

- Michigan wage and salary employment is forecast to grow modestly throughout the forecast period. However, Michigan wage and salary employment is expected to register its fourth straight year of decline (-1.1 percent) in 2004. In 2005, Michigan wage and salary employment is forecast to grow 0.3 percent with growth of 0.8 percent in 2006.
- The Michigan unemployment rate is forecast to fall to 6.7 percent for 2004. In 2005 and 2006, the Michigan unemployment rate is forecast to rise to 6.9 percent.
- Wage and salary income is forecast to increase 3.9 percent in 2005 and 4.3 percent in 2006. Personal income will post moderate increases throughout the forecast horizon. In 2005 and 2006, personal income is forecast to rise 4.2 percent and 5.4 percent, respectively.
- In FY 2005 and FY 2006, Michigan wage and salary income is expected to grow 3.0 percent and 4.2 percent. Disposable income is expected to rise 3.5 percent and 4.9 percent in FY 2005 and FY 2006, respectively.

Forecast Risks

- Nationally, employment has increased each month for sixteen months. However, Michigan job growth has remained elusive. The forecast projects moderate gains in Michigan employment. If businesses lose confidence in the expansion, both national and Michigan employment growth may be slower than forecast.
- Business investment is key to the continued economic expansion. If firms invest more than expected, growth may be stronger than forecast.
- Michigan manufacturing employment has declined sharply over the past few years. In 2004, Michigan manufacturing employment is expected to decline at a slightly slower rate than in 2003. Similarly, manufacturing declines are forecast to slow still further in 2005. If Big Three market share falls precipitously, manufacturing employment could decline more steeply.
- Continued higher oil and natural gas prices could curb growth. Weaker growth abroad could also slow domestic growth by reducing export growth.
- A rapidly falling dollar, while helping the manufacturing sector and exports, could also spur inflation and lead to instability for U.S. financial markets. Slower equity price growth or outright declines could slow consumption and investment spending.
- If firms add to their inventories faster (slower) than projected, economic growth will be more (less) rapid than projected.
- Geopolitical concerns continue to pose a risk to the forecast.

ECONOMIC REVIEW AND OUTLOOK
January 13, 2005

Current U.S. Economic Situation

Summary

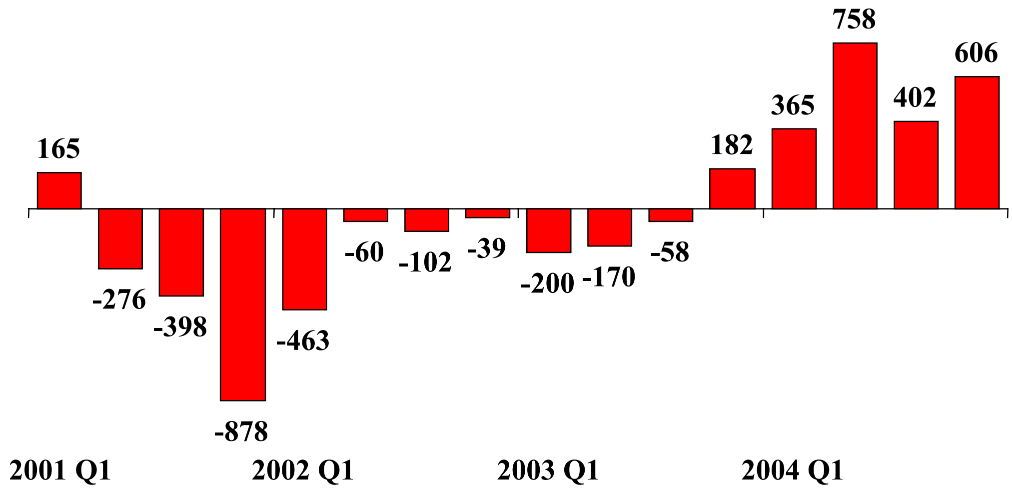
The current recovery is now over three years old, as dated by the National Bureau of Economic Research, having begun in November 2001. Over the past six quarters, real GDP growth has exceeded 3.0 percent each quarter. With the exception of the second quarter of 2004, consumption growth has been strong during the recovery. Similarly, with the exception of the first quarter of 2004, equipment and software investment has grown at double digit rates over the past year and a half, spurred by higher profits and tax incentives that expired at the end of 2004. Light vehicle sales have remained strong throughout the recovery, boosted by record incentives and low financing rates. Supported by historically low interest rates, new and existing home sales have remained strong as well.

Employment growth, however, has lagged the recovery. Employment declined each quarter during the recovery until the fourth quarter of 2003. While employment has grown in each of the past four quarters, that growth has been uneven. Employment reported tepid growth the last quarter of 2003 and moderate growth in the first quarter of 2004; employment then surged in the second quarter of this year before moderating in the third quarter. Employment recorded strong growth in October but more moderate growth in November and December. Despite recent growth, U.S. payroll employment remains a quarter million jobs below its March 2001 peak. Continued job growth will be key to sustained economic growth.

Interest rates have remained at historically low levels, but are expected to rise as the economy continues to report solid growth. Inflationary pressures will build with higher commodity prices and wage pressures as job growth increases. Energy prices, most notably oil, have increased due to a restricted supply and growing world demand. Oil prices have decreased from highs of $55 a barrel in late October to approximately $45 a barrel in early January. Security concerns for oil supplies are also in the forefront with tensions high in Iraq and other oil producing nations.

Federal government spending is expected to remain solid in the near-term with defense spending remaining robust through the middle of 2005. Federal government spending is then expected to slow as defense expenditure growth decelerates. State and local government spending is expected to remain weak through 2005 but begin to increase in 2006.

US Payroll Employment Growing
(Quarterly Change in Thousands)

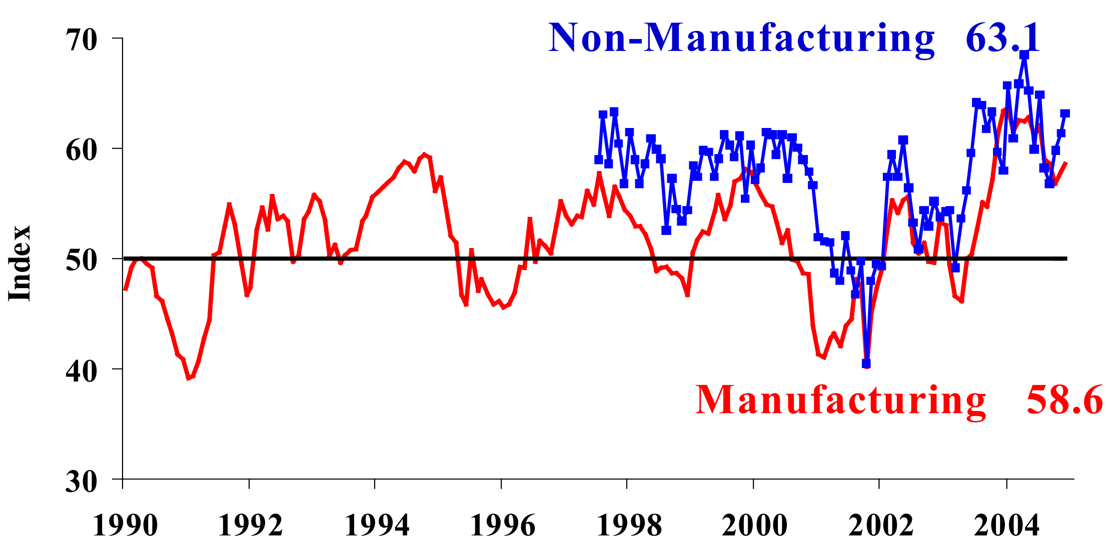


Source: U.S. Bureau of Labor Statistics

Major Economic Indicators

Major U.S. economic indicators point to continued, but likely slowing, economic growth. The Institute for Supply Management's (ISM) manufacturing index, while signaling continued growth, has been below 60 the past five months. The ISM non-manufacturing index rose in December and has been above 60 for the past two months. A reading of 50 indicates a growing sector.

ISM Indices Signal Growth in Manufacturing and Services



Source: Institute for Supply Management.

For over a year, new orders for durable goods have trended upward. However, in recent months, growth in new orders has moderated, disappointing expectations. Using a three-month trailing average, November 2004 new durable goods orders were 8.3 percent higher than a year ago. Capacity utilization remains near 20-year lows. After having trended upward earlier in 2004, capacity utilization growth has flattened out in recent months. Equipment investment has grown at faster than a 10 percent rate in five of the past six quarters.

While recent retail sales growth has been uneven, November 2004 retail sales were up 7.2 percent from a year ago. Consumer sentiment rose significantly in December 2004. Improving labor markets and declining energy prices contributed to the increase in December. The ABC News/Washington Post consumer comfort index, which measures consumers' attitude toward current economic conditions, has largely moved sideways since July 2004.

In November, the index of leading economic indicators rose after declining the previous five months.

Employment

U.S. employment has now increased every month since September 2003. However, this growth has been uneven. Employment grew at a tepid rate through the end of 2003 before posting moderate growth the first half of 2004. Employment growth then slowed over the summer before reporting strong growth in October. Despite employment growth for over a year, U.S. employment remains a quarter of a million jobs below the March 2001 peak and some sectors are still struggling.

The manufacturing sector has been particularly hard hit. Even before the recession, the manufacturing sector was losing jobs. Beginning in August 2000, U.S. manufacturing employment fell for 42 straight months. Manufacturing employment then reported solid gains in early 2004. However, in recent months, manufacturing employment has remained essentially unchanged. Over the past four years the manufacturing sector has lost nearly 3 million jobs. Rapid productivity gains allowed firms to reduce payroll employment even as they continued to increase output.

U.S. employment indicators are stronger and indicate that employment should continue to rise. Compared to a year ago, initial unemployment claims have fallen from around 360,000 to around 330,000 (four week moving average). Weekly initial unemployment claims have largely walked sideways since April 2004. At 333,000, the most recent four-week average of initial claims has returned to its pre-recession level.

The Institute for Supply Management's (ISM) manufacturing employment index component has shown expansion each month since late 2003. However, in the most recent month, the employment index fell to its lowest level since November 2003. The non-manufacturing ISM employment index has signaled expansion in 14 of the past 15 months. The Challenger Report count of announced layoffs rose in December 2004, up 17 percent from last year, to its highest level since January 2004. Overall layoff totals for 2004 were down 16 percent from 2003.

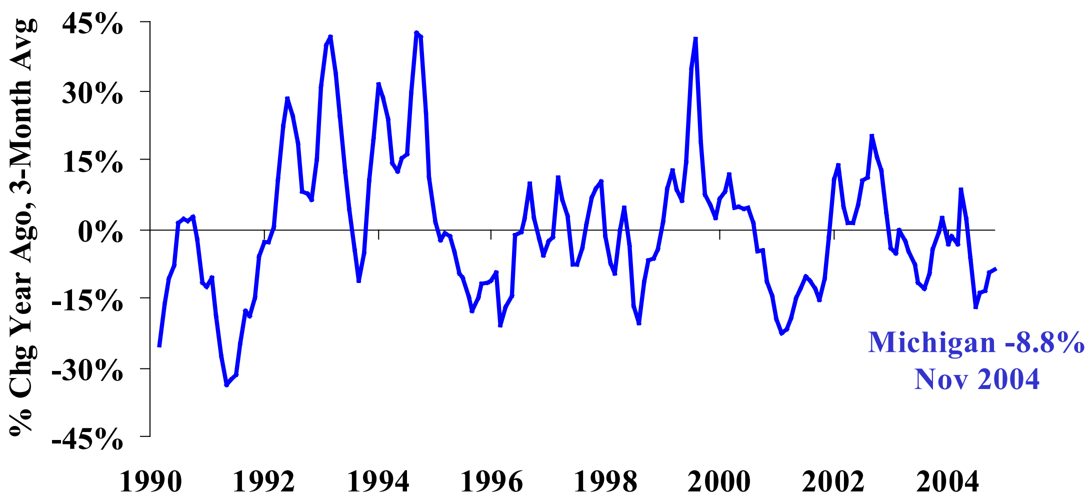
Weekly hours worked, a leading indicator for employment, have remained flat recently. The December 2004 reading showed average hours worked at 33.8 hours, up slightly from November.

Vehicle Sales and Production

Rebates coupled with low financing rates have helped maintain vehicle sales above 16 million units. In 2004, light vehicle sales averaged a projected 16.7 million units. Over the past few years, imports and transplants have continued to increase their market share. The traditional Big Three market share has continued to fall, with their share at 58.7 percent for 2004, a record low.

Averaged over the past three months, U.S. vehicle production in November 2004 has decreased 5.9 percent while Michigan vehicle production is down 8.8 percent.

Michigan Vehicle Production Down from Year Ago



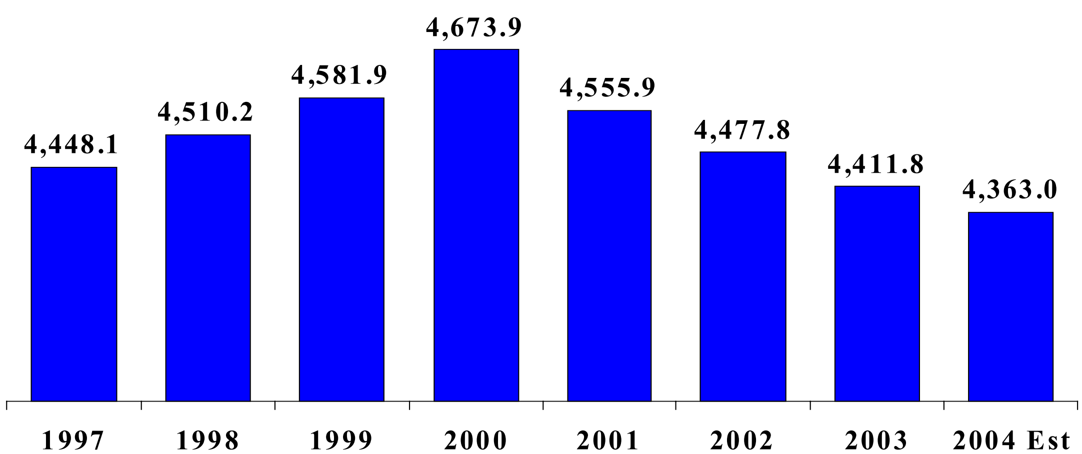
Source: Automotive News and Michigan Department of Treasury.

Current Michigan Economic Conditions

Employment

Michigan's economy relies heavily on the performance of the manufacturing sector in general and the auto industry specifically. Given extremely weak manufacturing employment performance, declining vehicle production, continued declines in Big 3 market share along with continued supply rationalization among vehicle suppliers, Michigan's employment performance has been below the national average. Substantial productivity gains in the vehicle industry have also contributed to Michigan's sub-par employment performance. Over the past three years, the annual average for wage and salary employment has fallen. Through November, state employment is down compared to a year ago. From Michigan's employment peak in June 2000 compared to November 2004, Michigan has lost 324,700 jobs. By this time after the 1990-1991 recession, Michigan employment had risen by about 200,000 jobs *above* its pre-recession peak.

Michigan Wage and Salary Employment Declines Past Four Years
(annual average in thousands)



Source: Bureau of Labor Statistics.

Michigan manufacturing employment has declined even more sharply. Since June 2000, Michigan manufacturing employment has fallen by more than 200,000 jobs. Michigan has lost more than one out of every five manufacturing jobs it had at the state's employment peak.

Unemployment Rate

Michigan's annual average unemployment rate for 2004 is forecast at 6.7 percent, down from 7.3 percent in 2003. The most recent monthly unemployment reading in November 2004 was 7.0 percent. The state's unemployment rate is down 0.6 percentage points from a year ago, but is substantially above the lows of around 3.0 percent achieved during the expansion of the late 1990s.

Personal Income

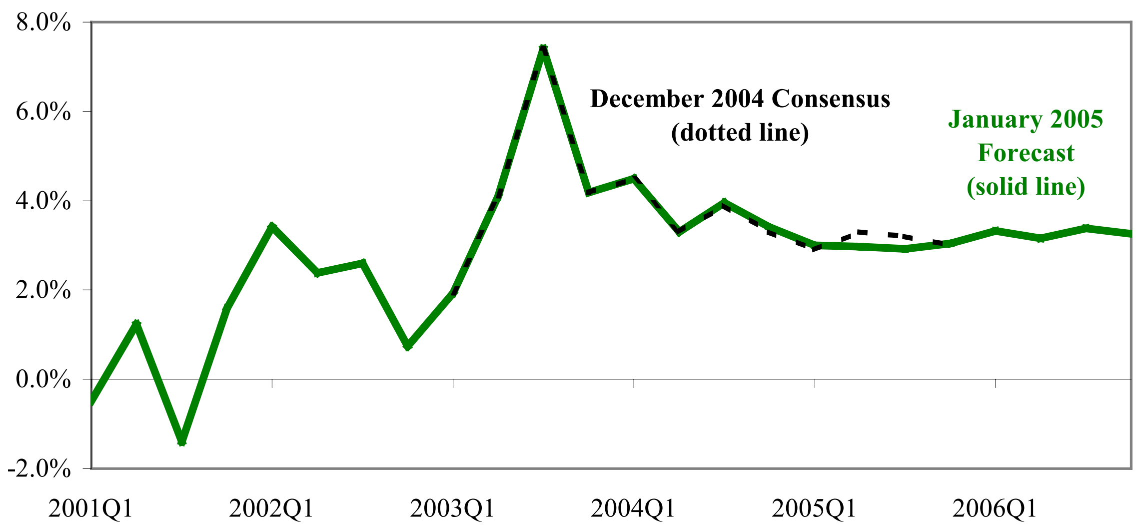
Michigan's personal income is expected to increase 2.7 percent in 2004; wages and salaries are forecast to grow 0.7 percent. Wages and salaries grew 1.7 percent year-over-year in the third quarter of 2004. Overall personal income grew 3.3 percent year over year in the third quarter. (Large contributions to employee pension and health insurance plans largely account for the apparent incongruity between overall personal income growth and wage and salary growth).

2005 and 2006 U.S. Economic Outlook

Summary

Real GDP is forecast to grow 3.2 percent in both 2005 and 2006. Real GDP is forecast to grow 4.4 percent in 2004.

Real GDP Forecast Comparisons

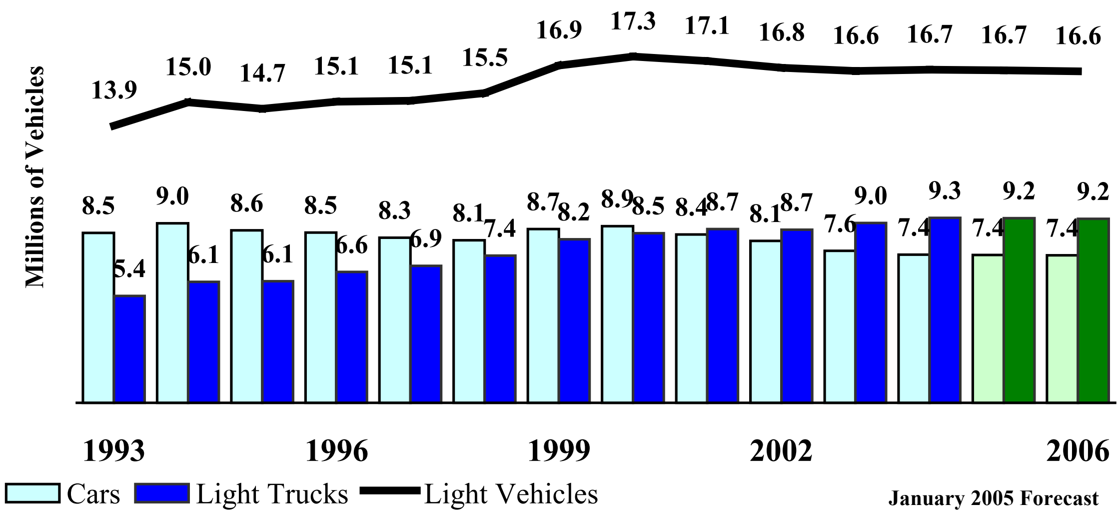


Business investment growth is forecast to increase 7.8 percent in 2005 and rise 5.6 percent in 2006. Low capacity utilization rates will be offset by the need to replace increasingly obsolete machinery and by higher profits that will allow companies to make investments. Consumption is forecast to rise 3.0 percent in 2005 and 3.4 percent in 2006. A stronger labor market will help consumer spending and offset the impact of higher interest rates. Government spending growth is expected to slow in 2005 and 2006. Federal defense spending growth will remain strong in 2005 before slowing in 2006. State and local government spending will increase, albeit at a weak rate in 2005, as some individual state economies make stronger recoveries. Net exports are forecast to fall in 2005 but rise slightly in 2006. Projected light vehicle sales are nearly unchanged from 2004 with projected sales of 16.7 million units in 2005 and 16.6 million units in 2006.

Inflation will remain moderate throughout the forecast horizon. As measured by the consumer price index (CPI), consumer prices are expected to rise 2.5 percent in 2005 and 2.4 percent in 2006. Interest rates are forecast to remain historically low even as the Federal Reserve continues to tighten.

U.S. employment is forecast to rise in 2005 and 2006 with gains projected throughout the forecast horizon. The U.S. unemployment rate is expected to fall slightly from 5.5 percent in 2004 to 5.4 percent in 2005 and remain at 5.4 percent in 2006.

Motor Vehicle Sales Stable



Source: Bureau of Economic Analysis, U.S. Department of Commerce, and Administration Forecast, January 2005.

<u>Assumptions</u>

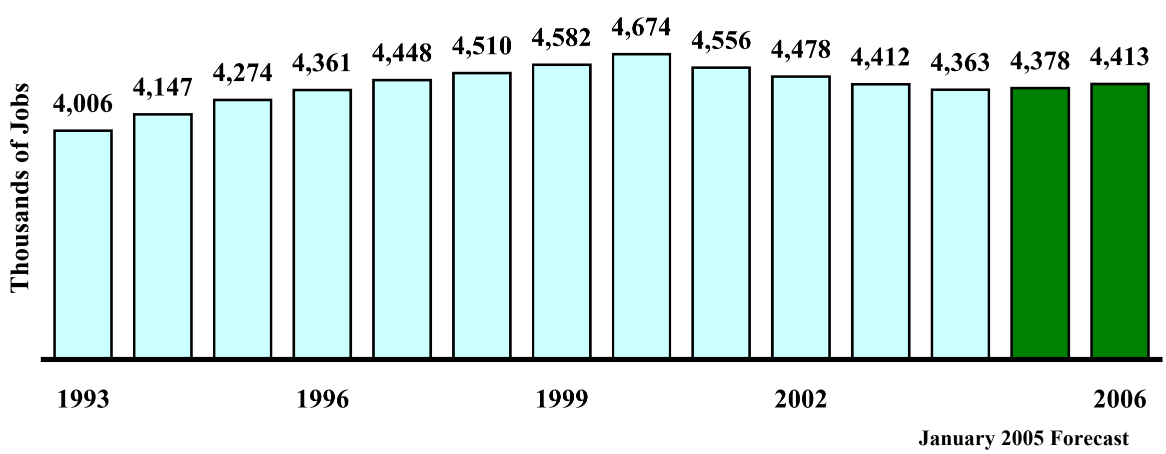
Oil prices are projected to decline to $38 a barrel by the end of 2005 and decline to the mid-thirties by 2006. With stronger employment readings and commodity price pressures, the Federal Reserve is expected to continue to increase the federal funds rate at a moderate pace.

The household savings rate is forecast to stay around 1.0 percent throughout the forecast. Stock prices are expected to post modest gains over the forecast horizon.

2005 and 2006 Michigan Economic Outlook

Michigan employment is forecast to decline in 2004 for the fourth straight year with modest growth in 2005 and in 2006. Weak growth in manufacturing employment will constrain Michigan employment increases. In 2005, employment is forecast to increase an average of 8,000 jobs per quarter and increase an average of 8,500 in 2006. Wage and salary employment is projected to increase 0.3 percent in 2005 and increase 0.8 percent in 2006. Michigan's unemployment rate is forecast to fall to 6.7 percent in 2004 before rising to 6.9 percent in 2005 and 2006.

Michigan Wage and Salary Employment



Source: Michigan Department of Labor and Economic Growth, U.S. Bureau of Labor Statistics and Administration Forecast, January 2005.

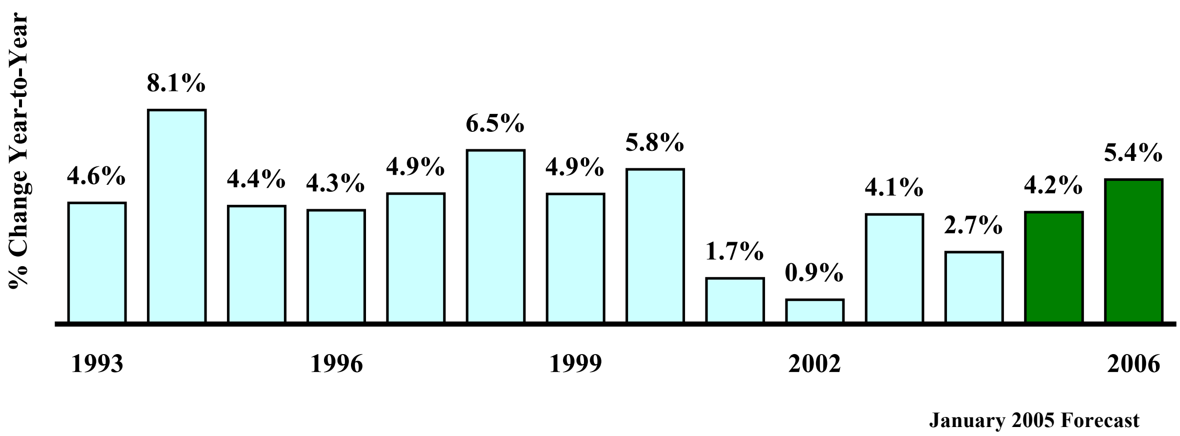
Wage and salary income is projected to rise 3.9 percent in 2005. In 2006, wage and salary income is projected to increase 4.3 percent as employment gains continue. Michigan personal income is forecast to rise 4.2 percent in 2005 and 5.4 percent in 2006.

Inflation, as measured by the Detroit CPI, is forecast to rise 2.5 percent in 2005 and 2.1 percent in 2006. As a result, real Michigan personal income (inflation adjusted) is expected to rise 1.7 percent in 2005 and 3.3 percent in 2006.

Table 1
Adminstration Economic Forecast
January 2005

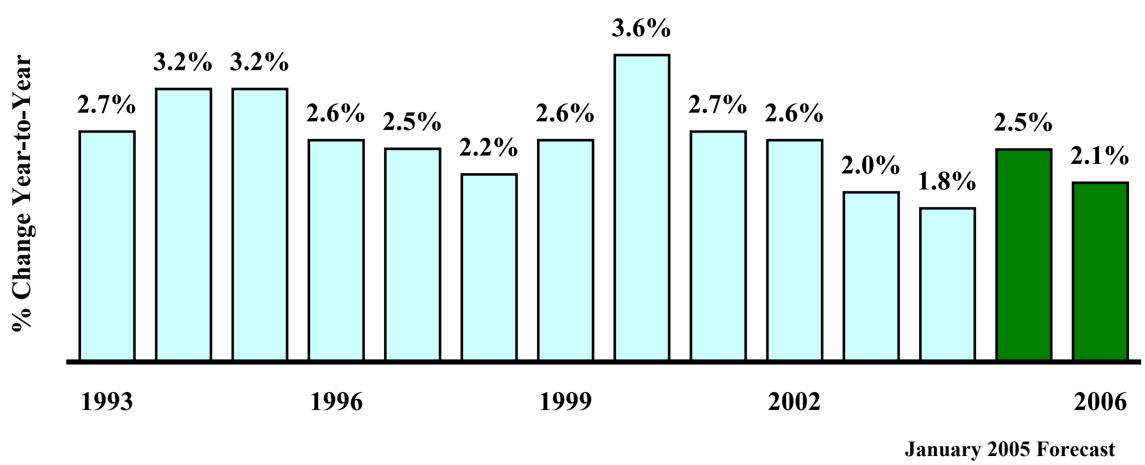
	Calendar 2003 Actual	Calendar 2004 Forecast	Percent Change from Prior Year	Calendar 2005 Forecast	Percent Change from Prior Year	Calendar 2006 Forecast	Percent Change from Prior Year
United States							
Real Gross Domestic Product (Billions of Chained 2000 Dollars)	$10,381	$10,838	4.4%	$11,185	3.2%	$11,540	3.2%
Implicit Price Deflator GDP (2000 = 100)	106.0	108.2	2.1%	110.6	2.2%	113.1	2.3%
Consumer Price Index (1982-84 = 100)	184.0	189.0	2.7%	193.7	2.5%	198.3	2.4%
Personal Consumption Deflator (2000 = 100)	105.5	107.7	2.1%	109.6	1.8%	111.8	2.0%
3-month Treasury Bills Interest Rate (percent)	1.0	1.4		2.8		3.8	
Aaa Corporate Bonds Interest Rate (percent)	5.7	5.6		6.0		6.6	
Unemployment Rate - Civilian (percent)	6.0	5.5		5.4		5.4	
Light Vehicle Sales (millions of units)	16.6	16.7	0.4%	16.7	-0.2%	16.6	-0.3%
Passenger Car Sales (millions of units)	7.6	7.4	-2.6%	7.4	-0.1%	7.4	-0.3%
Light Truck Sales (millions of units)	9.0	9.3	2.9%	9.2	-0.2%	9.2	-0.3%
Import Share of Light Vehicles (percent)	19.9	20.1		20.7		20.8	
Michigan							
Wage and Salary Employment (thousands)	4,412	4,363	-1.1%	4,378	0.3%	4,413	0.8%
Unemployment Rate (percent)	7.3	6.7		6.9		6.9	
Personal Income (millions of dollars)	$314,460	$322,950	2.7%	$336,543	4.2%	$354,837	5.4%
Real Personal Income (millions of 1982-84 dollars)	$172,307	$173,816	0.9%	$176,756	1.7%	$182,530	3.3%
Wages and Salaries (millions of dollars)	$176,493	$177,728	0.7%	$184,674	3.9%	$192,541	4.3%
Detroit Consumer Price Index (1982-84 = 100)	182.5	185.8	1.8%	190.4	2.5%	194.4	2.1%
Detroit CPI Fiscal Year (1982-84 = 100)	182.0	184.4	1.3%	189.3	2.7%	193.4	2.1%

Michigan Personal Income Growth Stronger in 2005



Source: Bureau of Economic Analysis, U.S. Department of Commerce, and Administration Forecast, January 2005.

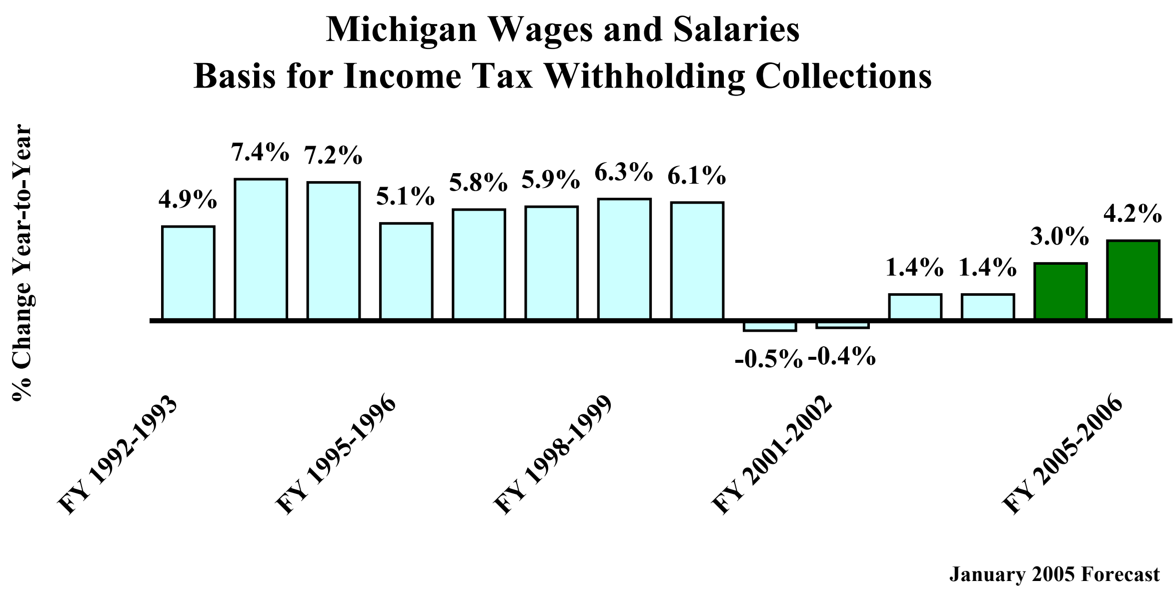
Inflation Rate Remains Low
Detroit CPI



Source: U.S. Bureau of Labor Statistics and Administration Forecast, January 2005.

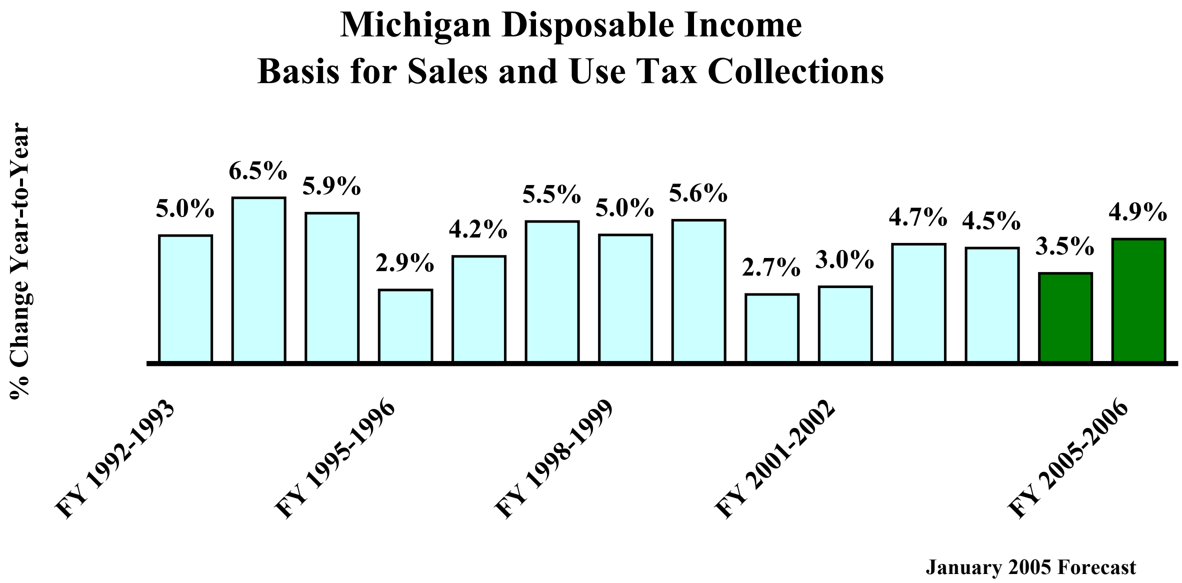
Fiscal Year Economics

Michigan's largest taxes are the individual income tax, which includes refunds, ($6.1 billion) and sales and use taxes ($8.4 billion). Income tax withholding is the largest income tax component. Withholding ($6.8 billion) is most affected by growth in wages and salaries. Michigan wages and salaries are expected to grow 3.0 percent in FY 2005 and to grow 4.2 percent in FY 2006. The FY 2005 and FY 2006 forecasted increases follow four consecutive years of slight declines or slight growth, and are substantially slower than growth reported through much of the 1990s.



Source: Bureau of Economic Analysis, U.S. Department of Commerce, and Administration Forecast, January 2005.

Sales and use taxes depend primarily on Michigan disposable (after tax) income and inflation. Disposable income is expected to rise 3.5 percent in FY 2005 and to increase 4.9 percent in FY 2006. The inflation rate is forecast to rise 2.7 percent in FY 2005 and is expected to increase 2.1 percent in FY 2006.



Source: Research Seminar in Quantitative Economics, University of Michigan, and Administration Forecast, January 2005.

Forecast Risks

U.S. employment has increased each month for over a year. However, employment at the national level is below the pre-recession peak and Michigan employment is still well below the previous employment peak. The baseline forecast predicts that sustained growth will spur U.S. employment increases in 2005 along with modest Michigan employment gains. If the employment gains do not materialize, economic growth will decline as consumer and business spending retrenches. If Michigan's employment level does not begin to increase soon, state economic growth will be below forecast levels.

If business investment is above projected levels, economic growth may be more than forecast. For the Michigan economy, Big Three market share is important. Sharp declines in market share would affect the Michigan economy adversely compared to other states. Similarly, faster (slower) productivity growth may increase (decrease) employment and overall economic growth. Faster (slower) inventory investment will increase (decrease) economic growth.

Higher oil and natural gas prices could curb growth. Weaker growth abroad could also slow domestic growth as exports grow more slowly. Equity prices are expected to rise modestly. Slower growth or outright declines could slow consumption and investment spending. If the U.S. dollar declines sharply, inflation risks would increase and financial markets may be roiled. Geopolitical concerns also pose a risk to the forecast.

ADMINISTRATION REVENUE ESTIMATES
January 13, 2005

Revenue Estimate Overview

The revenue estimates presented in this section consist of baseline revenues, revenue adjustments, and net revenues. Baseline revenues provide an estimate of the effects of the economy on tax revenues. For these estimates, FY 2004 is the base year. Any non-economic changes to the taxes occurring in FY 2005 and FY 2006 are not included in the baseline estimates. Non-economic changes are referred to in the tables as "tax adjustments." The net revenue estimates are the baseline revenues adjusted for tax adjustments.

This treatment of revenue is best illustrated with an example. Suppose tax revenues are $10.0 billion in a given year, and that based on the economic forecast, revenues are expected to grow by 5.0 percent per year. Baseline revenue would be $10.0 billion in Year 1, $10.5 billion in Year 2, and $11.0 billion in Year 3. Assume a rate cut is in place that would reduce revenues by $100 million in Year 1, $200 million in Year 2, and $300 million in Year 3. If Year 1 is the base year, the revenue adjustments for Year 1 would be $0 since the tax cut for this year is included in the base. The revenue adjustments for Year 2 would be $100 million, and the revenue adjustments for Year 3 would be $200 million, since the revenue adjustments are compared to the base year.

In the example above, the baseline revenues would be $10.0 billion, $10.5 billion, and $11.0 billion, for Years 1 through 3, respectively. The revenue adjustments would be $0 in Year 1, $100 million in Year 2, and $200 million in Year 3. The $200 million in Year 3 represents the tax cuts since Year 1. Net revenue would be $10.0 billion in Year 1, $10.4 billion in Year 2, and $10.8 billion in Year 3.

The revenue figures presented below are on a Consensus basis. Generally speaking, the Consensus estimates do not include certain one-time budget measures, such as withdrawals from the Budget Stabilization Fund, the sale of buildings, etc. The figures also assume the full statutory amount for revenue sharing payments. In addition, the estimates only include enacted legislation and do not include the effects of any proposed changes. The School Aid Fund estimates consist of taxes plus the transfer from the State Lottery Fund.

FY 2004 Revenue Review

FY 2004 GF-GP revenue totaled $8,042.0 million on a Consensus basis, a 1.0 percent increase over FY 2003. The FY 2004 GF-GP revenue total is $73.9 million above the December Consensus estimate. SAF revenue totaled $10,615.5 million, a 0.9 percent decline compared to FY 2003 (See Table 2). The FY 2004 SAF revenue total is $63.7 million above the December Consensus estimate. The changes from December were due to unanticipated tax adjustments relating to the FY 2004 book-closing process.

Table 2

FY 2003-04 Administration Revenue Estimates

(millions)

	Consensus December 3, 2004		Actual		
	Amount	**Growth**	**Amount**	**Growth**	**Change**
General Fund - General Purpose					
Baseline Revenue	$8,037.0		$7,910.9		
Tax Cut Adjustments	($68.9)		$131.2		
Net Resources	$7,968.1	0.1%	$8,042.0	1.0%	$73.9
School Aid Fund					
Baseline Revenue	$10,434.5		$10,532.0		
Tax Cut Adjustments	$117.3		$83.5		
Net Resources	$10,551.8	-1.5%	$10,615.5	-0.9%	$63.7
Combined					
Baseline Revenue	$18,471.5		$18,442.9		
Tax Cut Adjustments	$48.4		$214.7		
Net Resources	$18,519.9	-0.8%	$18,657.6	-0.1%	$137.7

Prepared By: Economic and Revenue Forecasting Division, Michigan Department of Treasury

FY 2005 Revenue Outlook

Baseline revenue growth improves in FY 2005 with the improving economy. FY 2005 GF-GP revenue is expected to be $7,869.8 million, a 1.7 percent baseline increase, and a 2.1 percent reduction after tax adjustments. Net GF-GP growth is slowed by a number of factors including the income tax rate cut, the continued phase-out of the state's estate tax, and the shift of some tobacco revenues to the Medicaid Trust Fund. The FY 2005 estimate is $31.2 million above the December Consensus estimate. SAF revenue is forecast to be $10,883.5 million, representing 3.2 percent SAF baseline growth and 2.5 percent growth after tax adjustments. The FY 2005 SAF estimate is essentially unchanged from the December Consensus estimate (See Table 3).

Table 3

FY 2004-05 Administration Revenue Estimates

(millions)

	Consensus December 3, 2004		Administration January 13, 2005		
	Amount	**Growth**	**Amount**	**Growth**	**Change**
General Fund - General Purpose					
Baseline Revenue	$8,222.9	2.3%	$8,048.7	1.7%	
Tax Cut Adjustments	($384.3)		($178.9)		
Net Resources	$7,838.6	-1.6%	$7,869.8	-2.1%	$31.2
School Aid Fund					
Baseline Revenue	$10,767.4	3.2%	$10,867.4	3.2%	
Tax Cut Adjustments	$116.0		$16.2		
Net Resources	$10,883.4	3.1%	$10,883.5	2.5%	$0.1
Combined					
Baseline Revenue	$18,990.3	2.8%	$18,916.1	2.6%	
Tax Cut Adjustments	($268.3)		($162.7)		
Net Resources	$18,722.0	1.1%	$18,753.4	0.5%	$31.4

Prepared By: Economic and Revenue Forecasting Division, Michigan Department of Treasury

FY 2006 Revenue Outlook

Revenue growth strengthens in FY 2006 as the economic recovery in Michigan takes hold. FY 2006 GF-GP revenue is expected to be $8,181.4 million, a 3.3 percent baseline increase, and a 4.0 percent increase after tax adjustments. Net GF-GP growth is increased by the shift of some tobacco tax revenues from the Medicaid Trust Fund back to GF-GP. SAF revenue is forecast to be $11,326.5 million, representing 4.0 percent SAF baseline growth and 4.1 percent growth after tax adjustments (see Table 4).

Table 4

FY 2005-06 Administration Revenue Estimates

(millions)

	Administration January 13, 2005	
	Amount	**Growth**
General Fund - General Purpose		
Baseline Revenue	$8,316.0	3.3%
Tax Cut Adjustments	($134.6)	
Net Resources	$8,181.4	4.0%
School Aid Fund		
Baseline Revenue	$11,306.6	4.0%
Tax Cut Adjustments	$19.9	
Net Resources	$11,326.5	4.1%
Combined		
Baseline Revenue	$19,622.6	3.7%
Tax Cut Adjustments	($114.7)	
Net Resources	$19,507.9	4.0%

Prepared By: Economic and Revenue Forecasting Division, Michigan Department of Treasury

Constitutional Revenue Limit

Article IX, Section 26, of the Michigan Constitution establishes a limit on the amount of revenue state government can collect in any given fiscal year. The revenue limit for a given fiscal year is equal to 9.49 percent of the state's personal income for the calendar year prior to the year in which the fiscal year begins. FY 2003 revenue is compared to CY 2001 personal income. If revenues exceed the limit by less than 1 percent, the state may deposit the excess into the Budget Stabilization Fund (BSF). If the revenues exceed the limit by more than 1 percent, the excess revenue is refunded to taxpayers via the income and single business taxes.

FY 2003 revenues were $4.6 billion below the revenue limit. State revenues will be well below the limit for FY 2004 through FY 2006 due to the effects of tax cuts and the economic slowdown on the state's revenue stream. FY 2004 revenues are expected to be $4.7 billion below the limit, FY 2005 revenues $5.7 billion below the limit, and FY 2006 revenues $5.6 billion below the limit (See Table 5).

Table 5

Administration Constitutional Revenue Limit Calculation

(millions)

	FY 2003	FY 2004	FY 2005	FY 2006
	Actual Mar 2004	Admin Jan 2005	Admin Jan 2005	Admin Jan 2005
Revenue Subject to Limit	$23,635.8	$24,088.1	$24,164.1	$25,082.2
Revenue Limit	**CY 2001**	**CY 2002**	**CY 2003**	**CY 2004**
Personal Income	$297,609	$303,745	$314,460	$322,950
Ratio	9.49%	9.49%	9.49%	9.49%
Revenue Limit	$28,243.1	$28,825.4	$29,842.2	$30,648.0
Amount Under (Over) Limit	**$4,607.3**	**$4,737.3**	**$5,678.2**	**$5,565.8**

Budget Stabilization Fund Calculation

The Management and Budget Act contains provisions for calculating a recommended deposit or withdrawal from the BSF. The calculation looks at personal income net of transfer payments adjusted for inflation. The change in this figure for the calendar year determines whether a pay-in or pay-out is dictated. If the formula calls for a deposit into the BSF, the deposit is made in the next fiscal year. If the formula calls for a withdrawal, the withdrawal is made during the current fiscal year.

If real personal income grows by more than 2 percent in a given calendar year, the fraction of income growth over 2 percent is multiplied by the current fiscal year's GF-GP revenue to determine the pay-in for the next fiscal year. If real personal income declines, the percentage deficiency under zero is multiplied by the current fiscal year's GF-GP revenue to determine the withdrawal available for the current fiscal year. If the change in real personal income is between 0 and 2 percent, no pay-in or withdrawal is indicated.

Real calendar year personal income for Michigan is expected to increase by 1.7 percent in 2005. Therefore, no pay-in is called for in FY 2006 (See Table 6).

Table 6

Budget and Economic Stabilization Fund Calculation Based on CY 2005 Personal Income Growth Administration Calculation

	CY 2004	CY 2005
Michigan Personal Income	$ 322,950 (1)	$ 336,543 (1)
less Transfer Payments	$ 48,905 (1)	$ 51,646 (1)
Income Net of Transfers	$ 274,045	$ 284,897
Detroit CPI	1.837 (2)	1.883 (3)
for 12 months ending	(June 2004)	(June 2005)
Real Adjusted Michigan Personal Income	$ 149,181	$ 151,276
Change in Real Adjusted Personal Income		1.4%
Between 0 and 2%		0.0%
GF-GP Revenue Fiscal Year 2004-2005		$ 7,869.8

	FY 2005-2006
BSF Pay-In Calculated for FY 2006	NO PAY-IN INDICATED

Notes:

(1) Personal Income and Transfer Payments, Administration Forecast, January 2005.

(2) Detroit Consumer Price Index, Average of 6 monthly values reported by BLS for each 12-month period.

(3) Detroit Consumer Price Index, Administration estimate.

School Aid Fund Revenue Adjustment Factor

The School Aid Fund (SAF) revenue adjustment factor for the next fiscal year is calculated by dividing the sum of current year and subsequent year SAF revenue by the sum of current year and prior year SAF revenue. For example, the FY 2006 SAF revenue adjustment factor is calculated by dividing the sum of FY 2005 and FY 2006 SAF revenue by the sum of FY 2004 and FY 2005 SAF revenue. The SAF revenue totals are adjusted for any change in the rate and base of the SAF taxes. The year for which the adjustment factor is being calculated is used as the base year for any tax adjustments. For FY 2006, the SAF revenue adjustment factor is calculated to be 1.0361 (See Table 7).

Table 7

Administration School Aid Revenue Adjustment Factor

For Fiscal Year FY 2006

	FY 2003-04	FY 2004-05	FY 2005-06
Baseline SAF Revenue	$10,532.0	$10,867.4	$11,306.6
Balance Sheet Adjustments	$83.5	$16.2	$19.9
Net SAF Estimates	$10,615.5	$10,883.5	$11,326.5
Adjustments to FY 2006 Base Year	($63.6)	$3.7	$0.0
Baseline Revenue on a FY 2006 Base	$10,551.9	$10,887.3	$11,326.5

School Aid Fund Revenue Adjustment Calculation for FY 2005-06

Sum of FY 2003-04 & FY 2004-05	$10,551.9	+	$10,887.3	=	$21,439.2
Sum of FY 2004-05 & FY 2005-06	$10,887.3	+	$11,326.5	=	$22,213.8

FY 2005-06 Revenue Adjustment Factor	**1.0361**

Note: Index is calculated off a FY 2006 base year.

Revenue Detail

The estimated tax and revenue totals include the effects of all enacted tax changes except sales tax savings resulting from reductions in revenue sharing payments to local units. The revenue totals by tax are presented separately for GF-GP and for the SAF (See Tables 8 and 9). Tax totals for the income, sales, use, and tobacco taxes for all funds are also included (See Table 10).

Table 8

Administration General Fund General Purpose Revenue Detail

(millions)

	FY 2004		FY 2005		FY 2006	
	Amount	Growth	Amount	Growth	Amount	Growth
GF-GP Tax Amounts						
Income Tax	$3,977.7	0.4%	$3,919.0	-1.5%	$4,091.3	4.4%
Sales	$102.2	60.3%	$117.2	14.7%	$112.3	-4.2%
Use	$877.4	7.1%	$912.8	4.0%	$953.0	4.4%
Cigarette	$242.7	-16.1%	$122.8	-49.4%	$235.6	91.8%
Beer & Wine	$51.5	0.8%	$52.0	1.0%	$52.5	1.0%
Liquor Specific	$33.0	6.1%	$33.5	1.5%	$34.0	1.5%
Single Business Tax	$1,827.6	-2.9%	$1,855.6	1.5%	$1,915.2	3.2%
Insurance Co. Premium	$230.3	-0.3%	$239.3	3.9%	$245.0	2.4%
Telephone & Telegraph	$101.3	-18.4%	$95.3	-5.9%	$79.3	-16.8%
Inheritance Estate	$75.5	-23.4%	$39.0	-48.3%	$0.0	-100.0%
Intangibles	$0.1	0.0%	$0.0	0.0%	$0.0	0.0%
Casino Wagering	$3.2	NA	$42.9	1240.6%	$42.9	0.0%
Horse Racing	$2.0	0.0%	$0.0	0.0%	$0.0	0.0%
Oil & Gas Severance	$57.1	7.1%	$55.0	-3.7%	$47.0	-14.5%
GF-GP Other Taxes	$24.0	-80.6%	$28.5	18.8%	$30.5	7.0%
Total GF-GP Taxes	$7,605.5	-0.7%	$7,512.9	-1.2%	$7,838.6	4.3%
GF-GP Non-Tax Revenue						
Federal Aid	$66.1	40.0%	$35.0	-47.0%	$35.0	0.0%
From Local Agencies	$2.9	222.2%	$2.0	-31.0%	$2.5	25.0%
From Services	$17.8	109.4%	$18.0	1.1%	$18.0	0.0%
From Licenses & Permit	$55.2	226.6%	$54.0	-2.2%	$54.0	0.0%
Miscellaneous	$76.0	-12.1%	$125.6	65.3%	$140.5	11.9%
Short Term Note Int.	$0.0	0.0%	$0.0	0.0%	$0.0	0.0%
Interfund Interest	($22.2)	66.9%	($73.0)	228.8%	($80.0)	9.6%
Liquor Purchase	$139.4	13.2%	$133.0	-4.6%	$134.0	0.8%
Charitable Games	$12.2	8.9%	$11.5	-5.7%	$11.0	-4.3%
Transfer From Escheats	$89.0	55.3%	$50.8	-42.9%	$27.8	-45.3%
Other Non Tax	$0.0	0.0%	$0.0	0.0%	$0.0	0.0%
Total Non Tax	$436.4	32.1%	$356.9	-18.2%	$342.8	-4.0%
Total GF-GP Revenue	$8,042.0	0.7%	$7,869.8	-2.1%	$8,181.4	4.0%

Table 9
Administration School Aid Fund Revenue Detail

	FY 2004		FY 2005		FY 2006	
	Amount	Growth	Amount	Growth	Amount	Growth
School Aid Fund						
Income Tax	$1,893.4	2.5%	$1,956.9	3.4%	$2,046.7	4.6%
Sales Tax	$4,716.7	0.8%	$4,887.8	3.6%	$5,109.3	4.5%
Use Tax	$439.1	7.0%	$456.5	3.9%	$476.6	4.4%
Liquor Excise Tax	$32.4	5.9%	$33.5	3.4%	$34.0	1.5%
Tobacco	$485.1	-0.5%	$479.9	-1.1%	$472.7	-1.5%
State Ed Prop Tax	$1,824.5	9.0%	$1,850.9	1.4%	$1,961.7	6.0%
Real Estate Transfer	$317.5	15.2%	$310.0	-2.4%	$310.0	0.0%
Ind and Comm Facilities	$150.2	-6.8%	$145.5	-3.1%	$150.5	3.4%
Casino (45% of 18%)	$95.8	5.4%	$98.0	2.3%	$96.3	-1.7%
Commercial Forest	$2.8	0.0%	$2.8	0.0%	$2.8	0.0%
Other Spec Taxes	$13.1	11.0%	$12.0	-8.4%	$12.0	0.0%
Subtotal Taxes	$9,970.6	3.1%	$10,233.8	2.6%	$10,672.6	4.3%
Lottery Transfer	$644.9	10.1%	$649.9	0.8%	$653.9	0.6%
Total SAF Revenue	$10,615.5	3.5%	$10,883.5	2.5%	$11,326.5	4.1%

Table 10

Administration Major Tax Totals

Major Tax Totals (Includes all Funds)						
Income Tax	$5,872.8	1.1%	$5,877.4	0.1%	$6,139.5	4.5%
Sales Tax	$6,473.5	0.8%	$6,707.8	3.6%	$7,010.0	4.5%
Use Tax	$1,316.5	7.0%	$1,369.3	4.0%	$1,429.6	4.4%
Cigarette and Tobacco	$992.8	11.4%	$1,188.8	19.7%	$1,171.5	-1.5%

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